

Message Text

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ACTION EB-04

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USMISSION EC BRUSSELS
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C O N F I D E N T I A L SECTION 01 OF 03 LONDON 06281

LIMDIS GREENBACK

DEPARTMENT PASS TREASURY FOR F.L. WIDMAN AND FRB

E.O. 11652: XGDS-1

TAGS: EFIN, UK

SUBJECT: U.K. VIEWS ON INTERNATIONAL MONETARY QUESTIONS

REF: A) EC BRUSSELS 3437; B) ROME 6000; C) EC BRUSSELS
3577

SUMMARY: FINANCIAL ATTACHES HAVE HAD DISCUSSIONS WITH H.
M. TREASURY AND BANK OF ENGLAND OFFICIALS CONCERNING EC
FINANCE MINISTERS MEETING AND INTERNATIONAL MONETARY TOP-
ICS. ACCORDING TO OFFICIALS, EC HAS AGREED TO APPROACH
U.S. PRIOR TO THE NEXT MEETING OF IMF INTERIM COMMITTEE
IN AN EFFORT TO WORK OUT AGREEMENT ON SEVERAL ISSUES,
INCLUDING DISCUSSION OF IMF QUOTA INCREASES AND TREATMENT
OF IMF GOLD. H.M. TREASURY AND BANK OF ENGLAND OFFICIALS
ALSO SEE CONTINUING, ALTHOUGH AT TIMES SPORADIC, PRESSURE
ON STERLING, IN PART DUE TO EC REFERENDUM, IN PART DUE TO
UNCERTAINTY ABOUT U.K. EXCHANGE RATE OBJECTIVES. END
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SUMMARY

1. RUNDOWN GIVEN US ON EC FINANCE COUNCIL APRIL 21 GENERALLY CONFIRMS REF C. U.K. DID NOT SEND A MINISTER, WAS REPRESENTED BY SIR DOUGLAS WASS. FOR THE U.K., THE MAJOR SUBSTANTIVE POINT WAS AGREEMENT BY ALL, INCLUDING THE FRENCH, TO APPROACH THE U.S. TO DISCUSS THE "NO NET GOLD PURCHASE" SCHEME. FRENCH HAD FOR SEVERAL MONTHS BEEN HOLDING UP APPROVAL OF EC APPROACH TO THE U.S. ON THIS SCHEME. OTHER EC MEMBERS WERE DETERMINED TO PUSH AHEAD WITH IT. WAY IS NOW SEEN AS CLEAR FOR G-10 TO DISCUSS THE ISSUE. SOURCES ALSO CONFIRM POSITION REPORTED IN REF B THAT MAJORITY OF EC COUNTRIES WOULD SUPPORT AN "ENABLING PROVISION" WHEREBY EXECUTIVE DIRECTORS WOULD BE GRANTED AUTHORITY TO SELL IMF GOLD TO MEMBERS AT MARKET RELATED PRICES WITH THE PROVISIO THAT THE CUMULATIVE STOCK OF OFFICIAL HOLDING WILL NOT INCREASE. U.K. OFFICIALS BELIEVE THAT FRANCE EXCLUDED, THE OTHER EIGHT WOULD ADOPT POSITIVE APPROACH IN AN ATTEMPT TO WORK OUT A JOINT AGREEMENT. NO MENTION MADE OF ITALIAN POSITION. SOURCE BELIEVED RAWLINSON IN WASHINGTON WELL INFORMED OF U.K. TREASURY VIEWS.

2. SOURCE SAID THERE WAS NO DISCUSSION OF IMF QUOTA QUESTIONS AT EC FINANCE COUNCIL. U.K. OFFICIALS RECOGNIZE STRONG U.S. OPPOSITION TO A QUOTA INCREASE WHICH WOULD RESULT IN A REDUCTION OF THE U.S. QUOTA SHARE BELOW 20 PERCENT, BUT THEY FEEL THIS IS INEVITABLE. THEY CITE THE NATURAL EROSION OF THE U.S. SHARE RESULTANT FROM ADDITIONAL COUNTRIES ASCRIBING TO FUND MEMBERSHIP. SWITZERLAND, THE PEOPLE'S REPUBLIC OF CHINA, BULGARIA, CZECHOSLOVAKIA AND HUNGARY WERE MENTIONED AS POSSIBLE NEW FUND MEMBERS IN THE FUTURE. IMF SOURCE HAS TOLD U.K. THAT THE THREE EASTERN EUROPEAN COUNTRIES MENTIONED HAVE BEEN EXPLORING MEMBERSHIP. POSSIBILITY OF ADDITIONAL OPEC QUOTA INCREASES IN FUTURE YEARS BEYOND THOSE ALREADY PROPOSED ALSO CITED.

3. WITH THIS IN MIND, U. K. OFFICIALS FEEL IT IS IN U.S. INTEREST TO ACCEPT, AT THIS TIME, A LOWER QUOTA SHARE COUPLED WITH AN ALTERATION OF IMF ARTICLES TO FACILITATE A 15 PERCENT BLOCKING VOTE ON ISSUES WHICH CURRENTLY RECONFIDENTIAL

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QUIRE A 20 PERCENT VETO. U.K. OFFICIALS APPEAR TO BE SYMPATHETIC TO U.S. POSITION BUT FEEL THAT THE 20 PERCENT SHARE LEVEL CANNOT BE MAINTAINED OVER TIME.

4. DURING DISCUSSION CONCERNING WORK OF WP-3, H.M. TREASURY OFFICIALS INDICATED THAT SIR DEREK MITCHELL'S FEBRUARY LETTER TO EMMINGER ON BALANCE OF PAYMENTS OBJECTIVES MAY HAVE BEEN OVERTAKEN BY EVENTS. LETTER WAS DRAFTED AT

LOW LEVELS IN H.M. TREASURY. ITS INITIAL MOTIVATION
STEMMED FROM U.K. FEARS OF CONTINUED WORLDWIDE ECONOMIC
DOWNTURN WITH MAJOR INDUSTRIAL COUNTRIES MOVING IN CYCLE.
THE U.S., GERMANY AND JAPAN ARE VIEWED AS CRUCIAL IN THIS
REGARD. H.M. TREASURY FORECASTERS BELIEVE THEY NOW SEE A

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LIMDIS GREENBACK - PASS FRB AND TREASURY

SHIFT TOWARDS A FOUR-YEAR WORLD TRADE CYCLE THAT COULD
BECOME INCREASINGLY VOLATILE IN ITS DOWNWARD AND UPWARD
SWINGS. WITH 1976 BEING A U.S. ELECTION YEAR, H.M. TREAS-
URY DOES NOT BELIEVE THAT ADDITIONAL INTERNATIONAL PRES-
SURE WILL BE REQUIRED TO GENERATE AN UPTURN WITH THE U.S.
GIVEN THE DOMESTIC FORCES THAT WILL ALSO BE WORKING IN
THIS DIRECTION. JAPAN CITED AS THE COUNTRY THAT HAS PROF-
ITED MOST FROM WHAT U.K. CONSIDERS REFUSAL TO ADEQUATELY
REFLATE. LOOKING AHEAD, SOURCES SAID THAT THE CONTEXT OF
THE MITCHELL LETTER MAY NOW BE APPROPRIATE IN TERMS OF HOW
TO DAMPEN THE WORLD TRADE BOOM WHICH THE U.K. EXPECTS TO
DEVELOP IN 1976 AND 1977, ADDING THAT LETTER COULD BE CON-
SIDERED AS SHOOTING AN ARROW INTO THE AIR, WONDERING WHERE

IT WOULD LAND.

5. ONE ASPECT OF THE U.S. ECONOMY WHICH DOES STILL CONCERN H.M. TREASURY IS THE LEVEL OF INTEREST RATES. WITH FEDERAL BUDGET DEFICIT AND EVENTUAL UPTURN EXPECTED IN THE U.S. THEY FEEL THAT RAPIDLY RISING RATES, IN PART DUE TO RESTRICTIVE U.S. MONETARY POLICY, COULD DELAY THE WORLD
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ECONOMIC TURNAROUND. THEY CITE THE IMPORTANCE OF U.S. RATES INTERNATIONALLY AND THE INABILITY OF THE U.K. TO ALTER ITS OWN RATES INDEPENDENTLY. SOME H.M. TREASURY OFFICIALS CONSIDER THAT HIGH U.K. DOMESTIC INTEREST RATES WOULD BE A DETRIMENT TO RECOVERY OF PRODUCTION INVESTMENT IN THE U.K.; OTHER SOURCES CONSIDER THAT U.K. INVESTMENT WILL NOT PICK UP IN ANY CASE UNTIL THE ECONOMY HAS ACTUALLY BEGUN TO SHOW POSITIVE SIGNS OF RECOVERY, REGARDLESS OF LEVEL OF U.K. DOMESTIC INTEREST RATES.

6. OFFICIAL CONCERNED WITH PERFORMANCE OF STERLING IN THE EXCHANGE MARKETS REFERRED TO LAST WEEKEND'S PRESS REPORTS THAT THE CHANCELLOR WOULD BE WILLING TO LET THE EXCHANGE RATE FALL AS "A PITY." IT WAS NOT AN INSPIRED LEAK AND IT HAS MADE H.M. TREASURY'S TASK IN DEFENDING THE RATE MORE DIFFICULT. SOURCE DID NOT DENY THAT U.K. MIGHT HAVE BEEN WILLING TO ALLOW RATE TO FALL SLOWLY AND STEADILY OVER TIME, BUT WAS VERY DISTRESSED THAT THIS OPTION SHOULD NOW BE CONSIDERED BY THE EXCHANGE MARKET TO BE H.M. TREASURY POLICY, ESPECIALLY GIVEN FIVE BILLION POUNDS HELD IN OFFICIAL EXCHANGE RESERVES BY FOREIGN COUNTRIES AND U.K. HOPE OF INDUCING ADDITIONAL INFLOWS FROM OPEC COUNTRIES. BANK OF ENGLAND HAS BEEN SUPPORTING THE RATE THIS WEEK WITH SOME COST TO RESERVES. LOOKING AHEAD, BANK OF ENGLAND AND FOREIGN EXCHANGE MARKET SOURCES CONSIDER THAT STERLING WILL COME UNDER PRESSURE IN THE RUN UP TO THE EC REFERENDUM, IF ONLY BECAUSE OF THE UNCERTAINTY ENGENDERED BY IT. SOURCES IN MAJOR CLEARING EXCHANGE BANKS CONSIDER THAT IF THE VOTE IS NEGATIVE, THERE COULD BE A RUN OR AT LEAST HEAVY PRESSURE ON STERLING AS A RESULT. NO OBJECTIVE FINANCIAL REASONS ARE GIVEN BUT RATHER "MARKET PSYCHOLOGY" COUPLED WITH BELIEF THAT BRITAIN IN LEAVING THE EC WOULD ALSO HAVE LEFT SOME FORM OF PROTECTIVE ASSOCIATION AND BE MORE VULNERABLE.

7. H.M. TREASURY'S REACTION TO THE CONSUMER PRODUCER PREP CON WAS THAT ON BALANCE THE MEETINGS HAD DAMAGED FRENCH REPUTATION, BUT WERE USEFUL IN POINTING UP THE DIFFICULTIES IN ANY NEGOTIATION BETWEEN CONSUMERS AND PRODUCERS. THE H.M. TREASURY OFFICIAL WHO ATTENDED PREP CON DESCRIBED IT AS A BLOODY MESS AND THOUGHT U.S. DELEGATES HAD BEEN

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VERY RESTRAINED IN THEIR REACTIONS.

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LIMDIS RESEARCH

8. IN-HOUSE, H.M. TREASURY REACTIONS TO THE BUDGET ARE MIXED BUT GENERALLY FAVORABLE. SENIOR OFFICIALS IN THE BANK OF ENGLAND ARE SKEPTICAL THAT THE CHANCELLOR WILL BE ABLE TO CUT PUBLIC EXPENDITURE NEXT YEAR AND FURTHER REDUCE THE PUBLIC SECTOR BORROWING REQUIREMENT TO THE EXTENT FORECAST IN THE BUDGET. H.M. TREASURY CAREER STAFF GIVE THE CHANCELLOR HIGH MARKS FOR HIS COMPREHENSION OF THE PROBLEMS AND WILLINGNESS TO FACE THEM, IN CONTRAST SAY TO PREVIOUS CHANCELLOR BARBER. SOURCES SAID THEY PREPARED BRIEFS FOR THE CHANCELLOR ARGUING AGAINST THE IMPO-

SITION OF IMPORT CONTROLS (AN OPTION WHICH WAS GIVEN SERIOUS CONSIDERATION). THE BRIEFS STRESSED THAT THE U.S. AS WELL AS EC PARTNERS MIGHT RETALIATE. H.M. TREASURY SOURCES CONSIDER THAT CONTINUING U.S. PRESSURE AND COMMENTS ABOUT DANGERS OF IMPORT CONTROLS AND POSSIBLE RETALIATION, BOTH IN PUBLIC AND IN PRIVATE TO THE CHANCELLOR, WILL BE USEFUL AND A CONSTRUCTIVE COUNTERWEIGHT TO THE ADVICE HE HEARS FROM OTHER SOURCES. ONE OF THESE OTHER SOURCES IS PROFESSOR LORD NICHOLAS KALDOR WHO IS NOW ENSCONCED IN CONFIDENTIAL

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H.M. TREASURY AS A SPECIAL ADVISOR TO THE CHANCELLOR. KALDOR TOLD FINANCIAL ATTACHES HE BELIEVES BRITAIN IS A LOW GROWTH/LOW PRODUCTIVITY ECONOMY WHICH NEEDS EXPORT INCENTIVES AND IMPORT RESTRICTIONS IN ORDER TO GIVE U.K. INDUSTRIAL STRUCTURE TIME TO REBUILD TO MEET INTERNATIONAL COMPETITION, WHICH IT CANNOT NOW DO.

RICHARDSON

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